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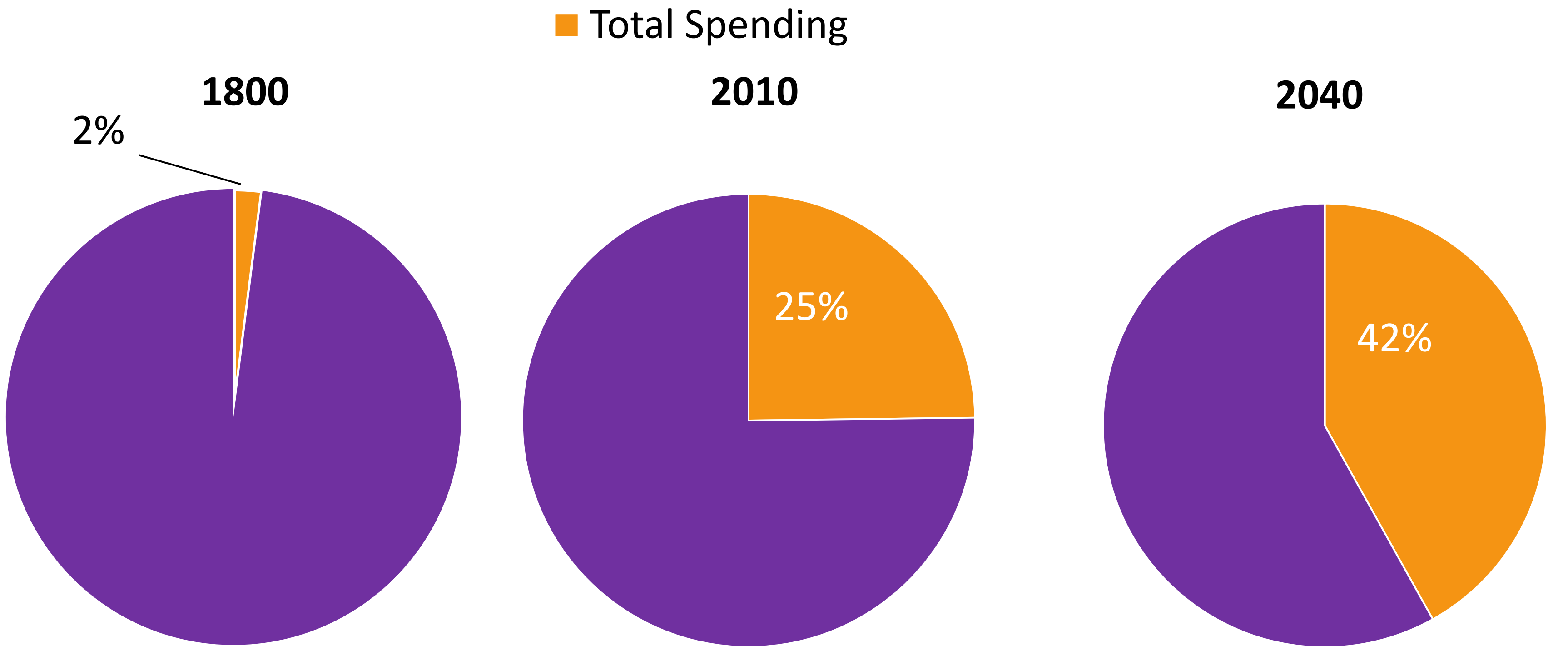
Our National Fiscal Challenge

August 12, 2010
Town Hall with Congressman Jim Himes
New Canaan, CT

David M. Walker
President and CEO
The Peter G. Peterson Foundation
and
Former Comptroller General of the United States

Total Federal Spending

(As Percentage of U.S. Economy)

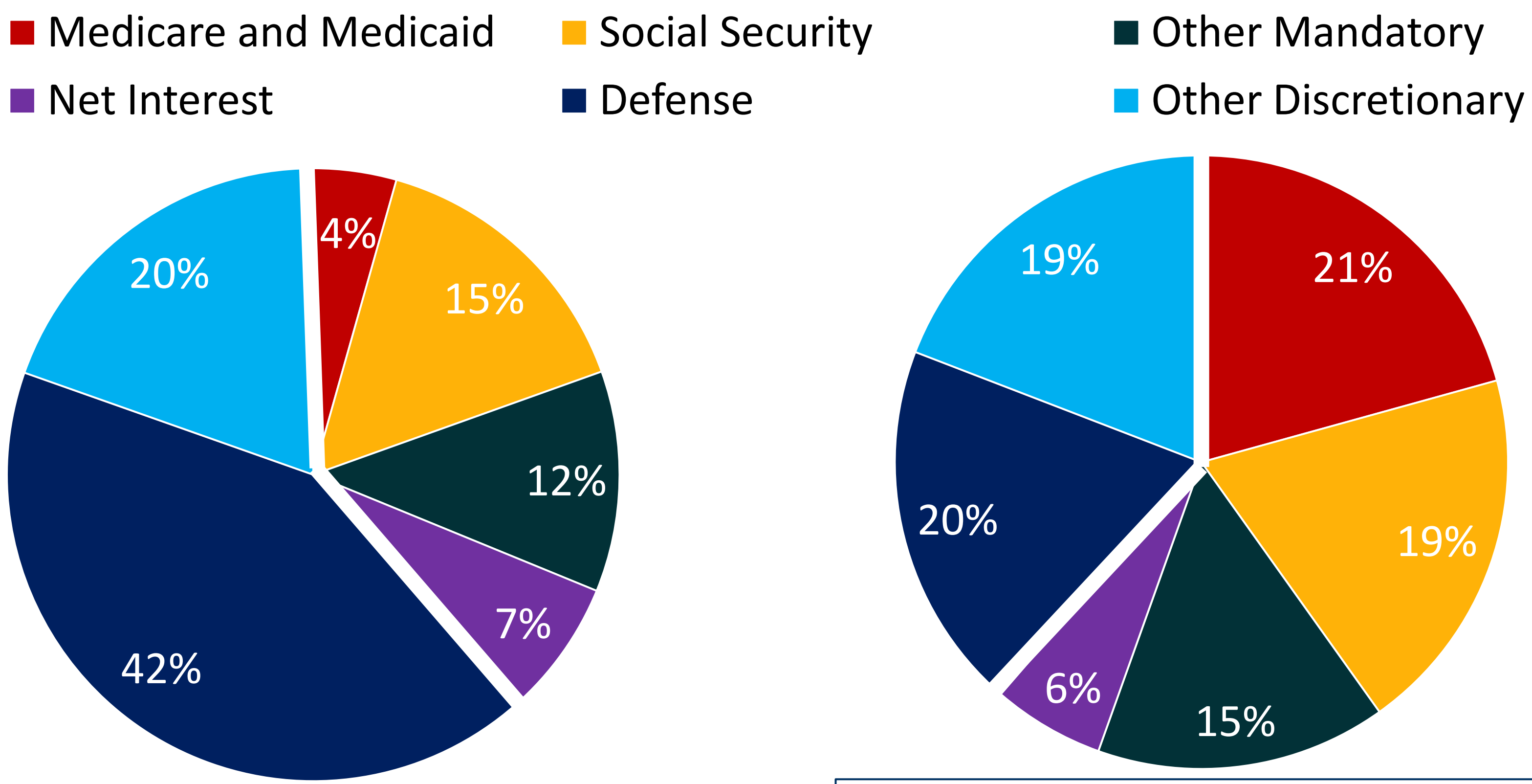


Size of the Total Economy: $8.8 Billion (Constant 2009 Dollars)	Projected Size of the Total Economy: $14.5 Trillion (Constant 2009 Dollars)	Projected Size of the Total Economy: $29.4 Trillion (Constant 2009 Dollars)

SOURCES: Data from the Congressional Budget Office, *Preliminary Analysis of the President's Budget*: March 2010; and Government Accountability Office *The Federal Government's Long-Term Fiscal Outlook*: January 2010 Update. Compiled by PGPF.

Composition of Federal Spending

(% of Total Spending)

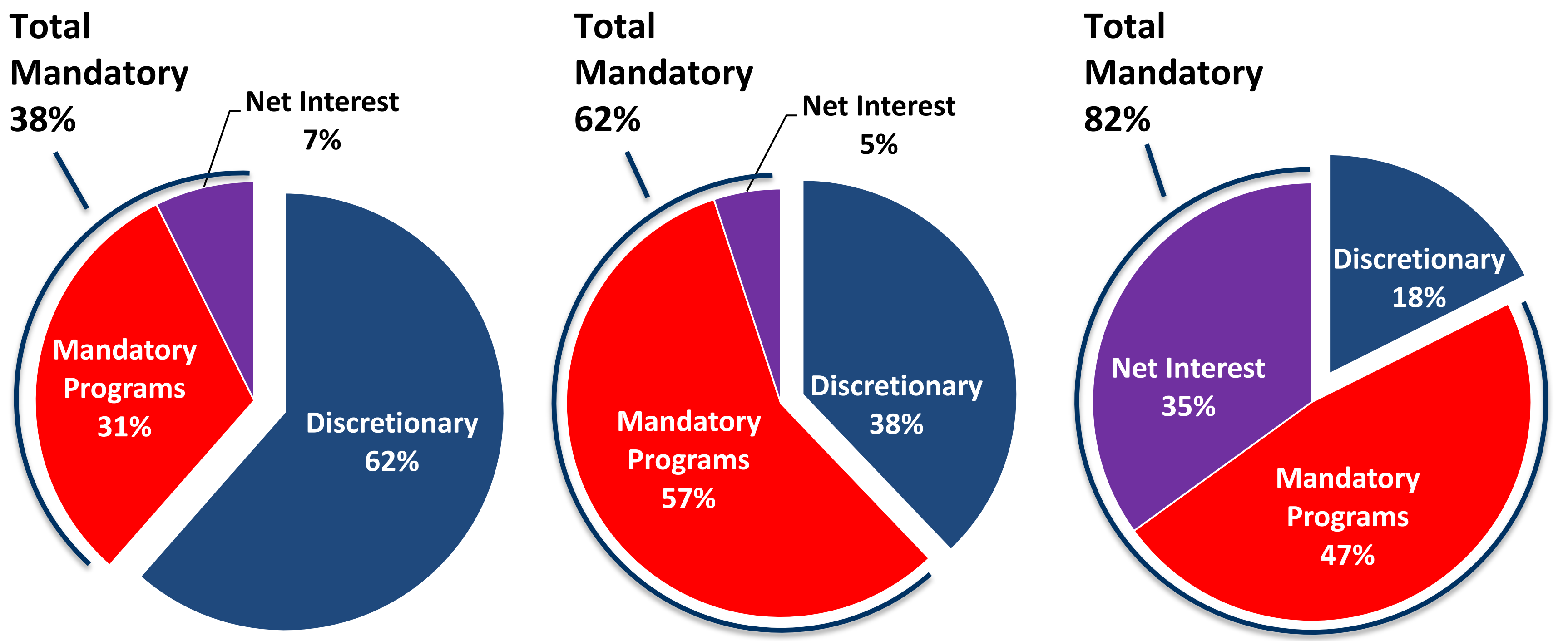


Total Spending 1970:
$900 Billion (Constant 2009 Dollars)

Total Spending 2010 (estimated):
$3.5 Trillion (Constant 2009 Dollars)

SOURCES: Data from the Office of Management and Budget, *A New Era of Responsibility: The 2011 Budget*, Historical Tables; and the Congressional Budget Office, *Preliminary Analysis of the President's Budget*: March 2010. Compiled by PGPF.

Mandatory programs and interest costs are taking over more and more of the federal budget, crowding out important discretionary programs



Total Spending 1970: $900 Billion

Total Spending 2010: $3.5 Trillion (est.)

Total Spending 2040: $12.3 Trillion (est.)

SOURCES: Data derived from the Office of Management and Budget, *FY 2011 Budget, Historical Tables*, February 2010; and the Government Accountability Office, *The Federal Government's Long-Term Fiscal Outlook,* January 2010 Update, alternative simulation using Congressional Budget Office assumptions. Calculated by PGPF.

Notes: Data is in constant 2009 dollars. Mandatory programs include Social Security, Medicare, Medicaid and other entitlement programs.

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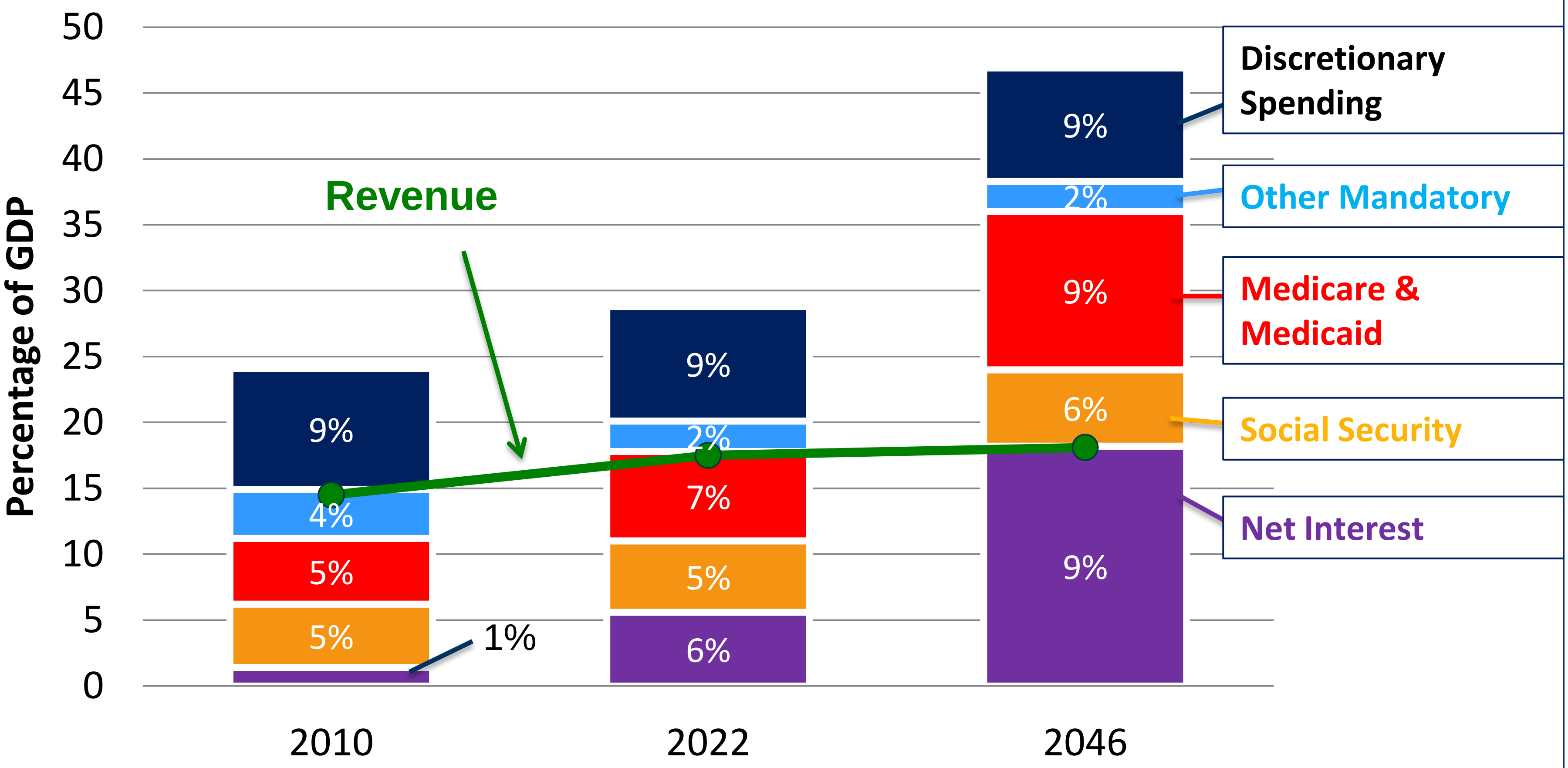
The following table illustrates the U.S. government's explicit liabilities, commitments, and unfunded social insurance promises

	In Trillions of Dollars 2000	2009
Explicit liabilities	**$6.9**	**$14.1**
Publicly held debt	3.4	7.6
Military & civilian pensions & retiree health	2.8	5.3
Other Major Fiscal Exposures	0.7	1.3
Commitments & contingencies	**0.5**	**2.0**
E.g., Pension Benefit Guaranty Corporation, undelivered orders		
Social insurance promises	**13.0**	**45.8**
Future Social Security benefits	3.8	7.7
Future Medicare benefits	9.2	38.2
Future Medicare Part A benefits	2.7	13.8
Future Medicare Part B benefits	6.5	17.2
Future Medicare Part D benefits	--	7.2
Total	**$20.4**	**$61.9**

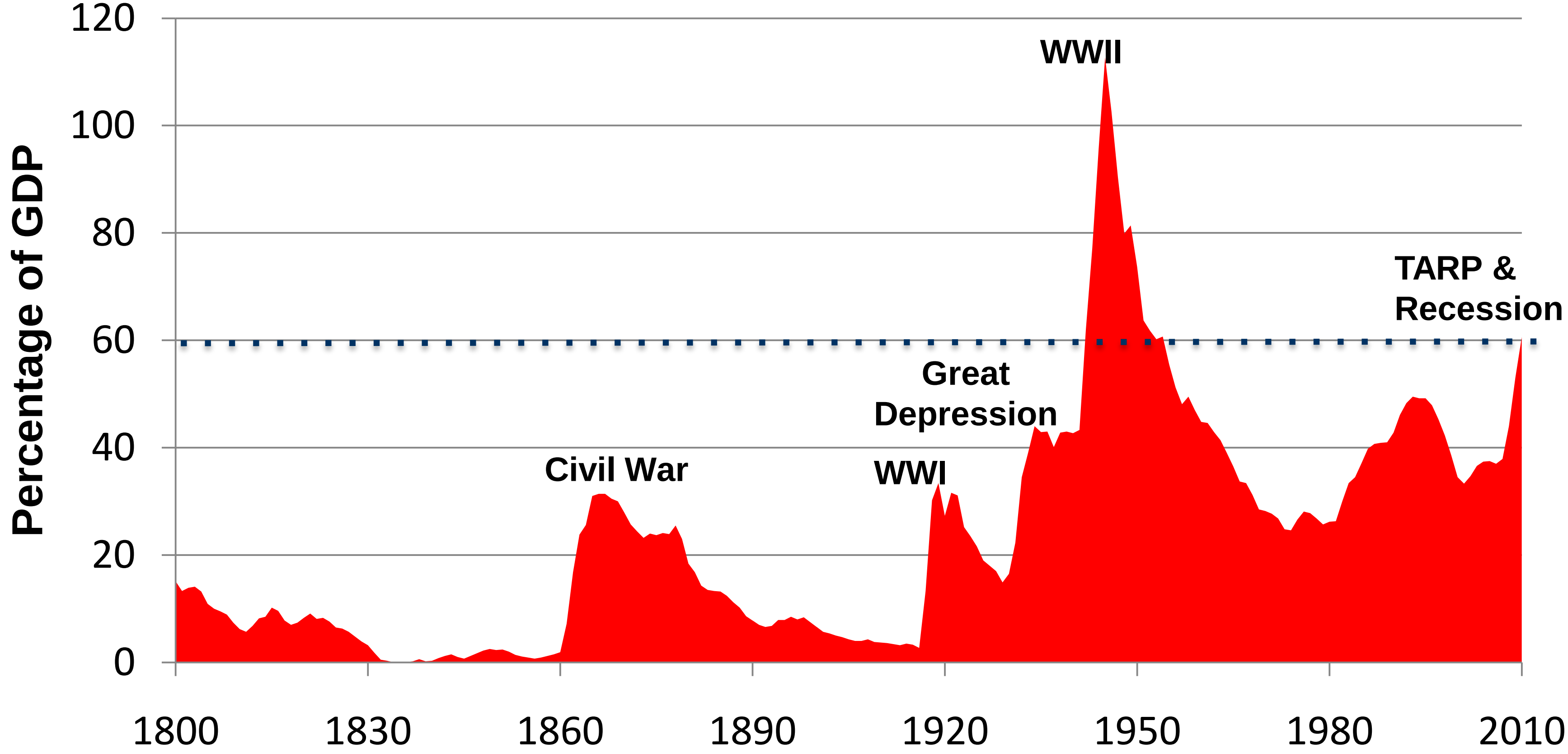
SOURCE: Data from the Department of Treasury, *2009 Financial Report of the United States Government*. Compiled by PGPF.
NOTE: Numbers may not add due to rounding. Estimates for Medicare and Social Security benefits are from the Social Security and Medicare Trustees reports, which are as of January 1, 2009 and show social insurance promises for the next 75 years. Future liabilities are discounted to present value based on a real interest rate of 2.9 percent and CPI growth of 2.8 percent. The totals do not include liabilities on the balance sheets of Fannie Mae, Freddie Mac, and the Federal Reserve. Assets of the U.S. government not included. Does not include civil service and military retirement funds, unemployment insurance, and debt held by other government accounts outside of Social Security and Medicare.

Without reforms, by 2022, future revenues will only cover Social Security, Medicare, Medicaid, and interest on the debt. By 2046, revenues won't even cover interest costs.



SOURCE: Data from the Government Accountability Office *The Federal Government's Long-Term Fiscal Outlook: January 2010 Update*, alternative simulation using Congressional Budget Office assumptions. Compiled by PGPF.
NOTE: Baseline interest rate is assumed to be 5.0 percent.

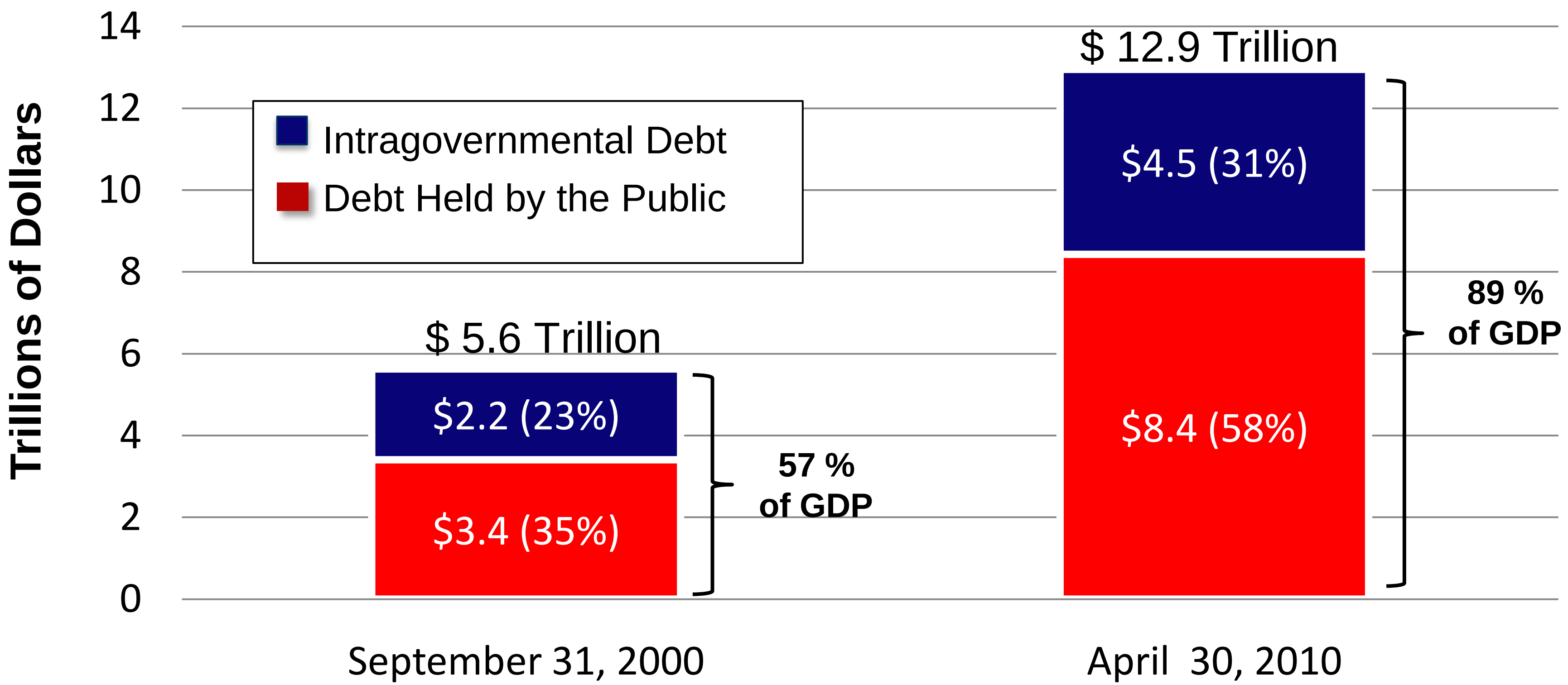
Since 1800, U.S. Debt Held by the Public has exceeded 60 percent of GDP (the debt level standard used by the European Union) only during World War II



SOURCES: Data from the Congressional Budget Office, *Long-Term Budget Outlook: June 2009;* the Government Accountability Office, *The Federal Government's Long-Term Fiscal Outlook*: January 2010 Update, alternative simulation using Congressional Budget Office assumptions. Compiled by PGPF.

NOTE: Debt held by the public refers to all federal debt held by individuals, corporations, state or local governments, and foreign entities.

The total debt includes debt held by the public (domestic and foreign investors) and debt the government owes to various government programs*



SOURCES: Data from the Office of Management and Budget, *A New Era of Responsibility: The 2011 Budget*: February 2010, Historical Tables; and the Department of Treasury, *Daily Treasury Statement* (April 30, 2010). Compiled by PGPF.

NOTE: Totals may not add due to rounding.

*Intragovernmental debt refers to Treasury securities held by federal trust funds (e.g., Social Security and Medicare) and other government accounts. Debt held by the public refers to all federal debt held by individuals, corporations, state or local governments, and foreign entities.

U.S. dependency on foreign lenders to finance the public debt has risen sharply

1970
Total Debt: $283 billion

Foreign Holdings: 5%

1990
Total Debt: $2,412 billion

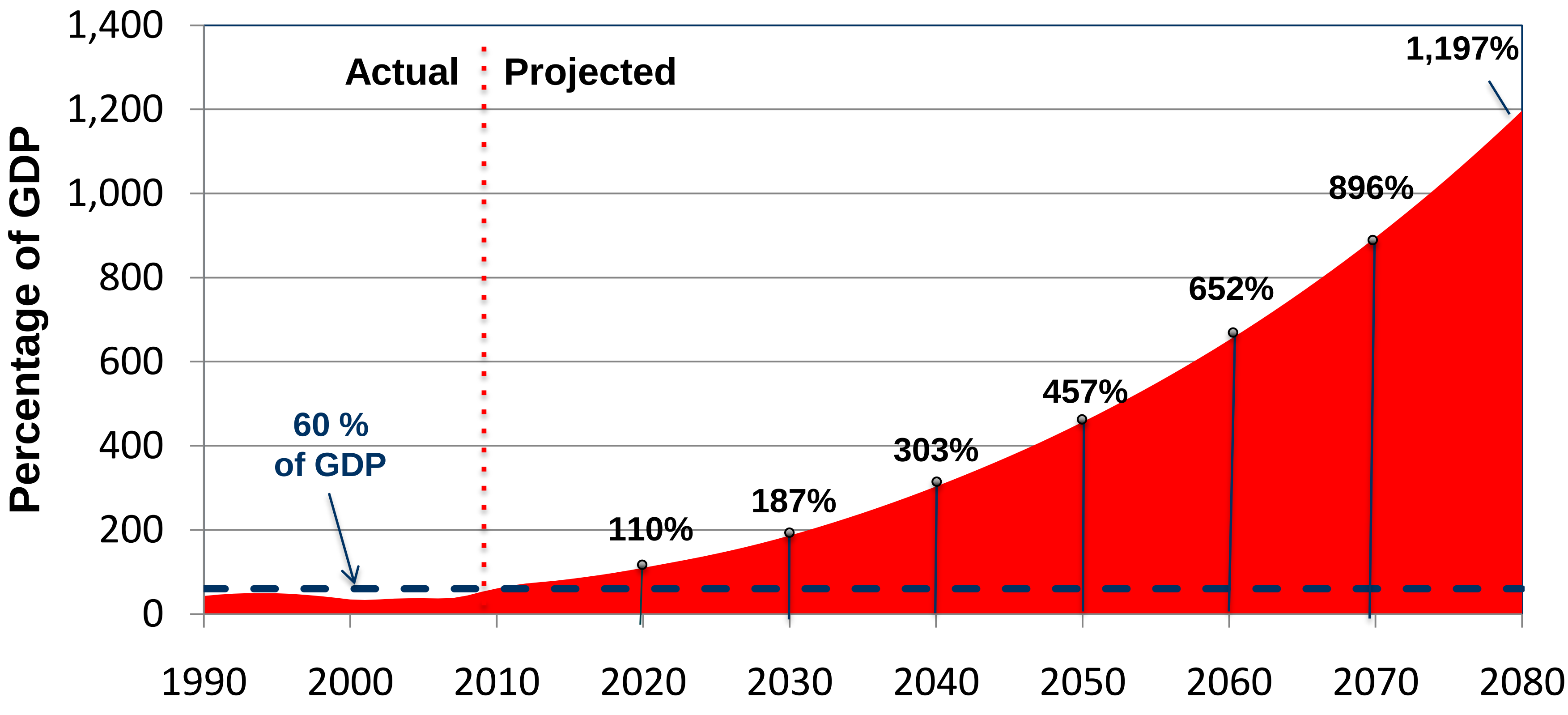
Foreign Holdings: 19%

2010 est.
Total Debt: $8,387 billion

Foreign Holdings: 47%

SOURCES: Data for 1970 and 1990 from the Office of Management and Budget, *A New Era of Responsibility: The 2011 Budget,* Analytical Perspectives, February 2010. Data for 2010 from Department of Treasury, *Daily Treasury Statement* (February 26, 2010) and Treasury International Capital Reporting System, April 15, 2010 release. Compiled by PGPF.
NOTE: 2010 data reflects debt levels through February 2010.

Future U.S. debt held by the public is projected to soar if current policies remain unchanged



SOURCES: Data from the Congressional Budget Office, *Long-Term Budget Outlook* (June 2009); the Government Accountability Office, *The Federal Government's Long-Term Fiscal Outlook: January 2010 Update*, alternative simulation using Congressional Budget Office assumptions. Compiled by PGPF.

NOTE: Debt held by the public refers to all federal debt held by individuals, corporations, state or local governments, and foreign entities.

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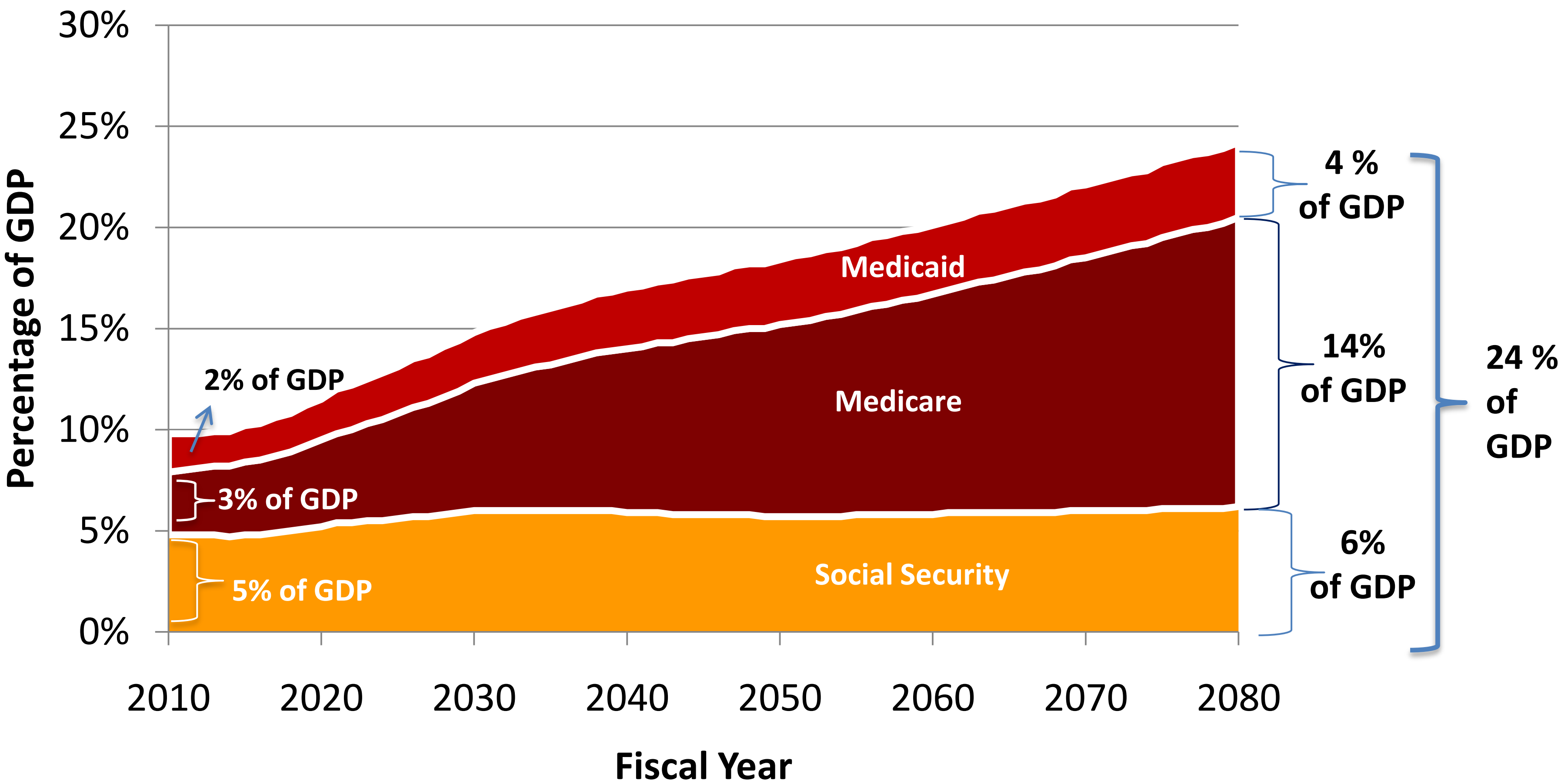
Social Security, Medicare, and Medicaid, the three largest entitlement programs, are projected to more than double as a percentage of GDP under current policies



SOURCE: Data from the Government Accountability Office, *The Federal Government's Long-Term Fiscal Outlook*: *January 2010 Update*, alternative simulation using Congressional Budget Office Assumptions. Compiled by PGPF.

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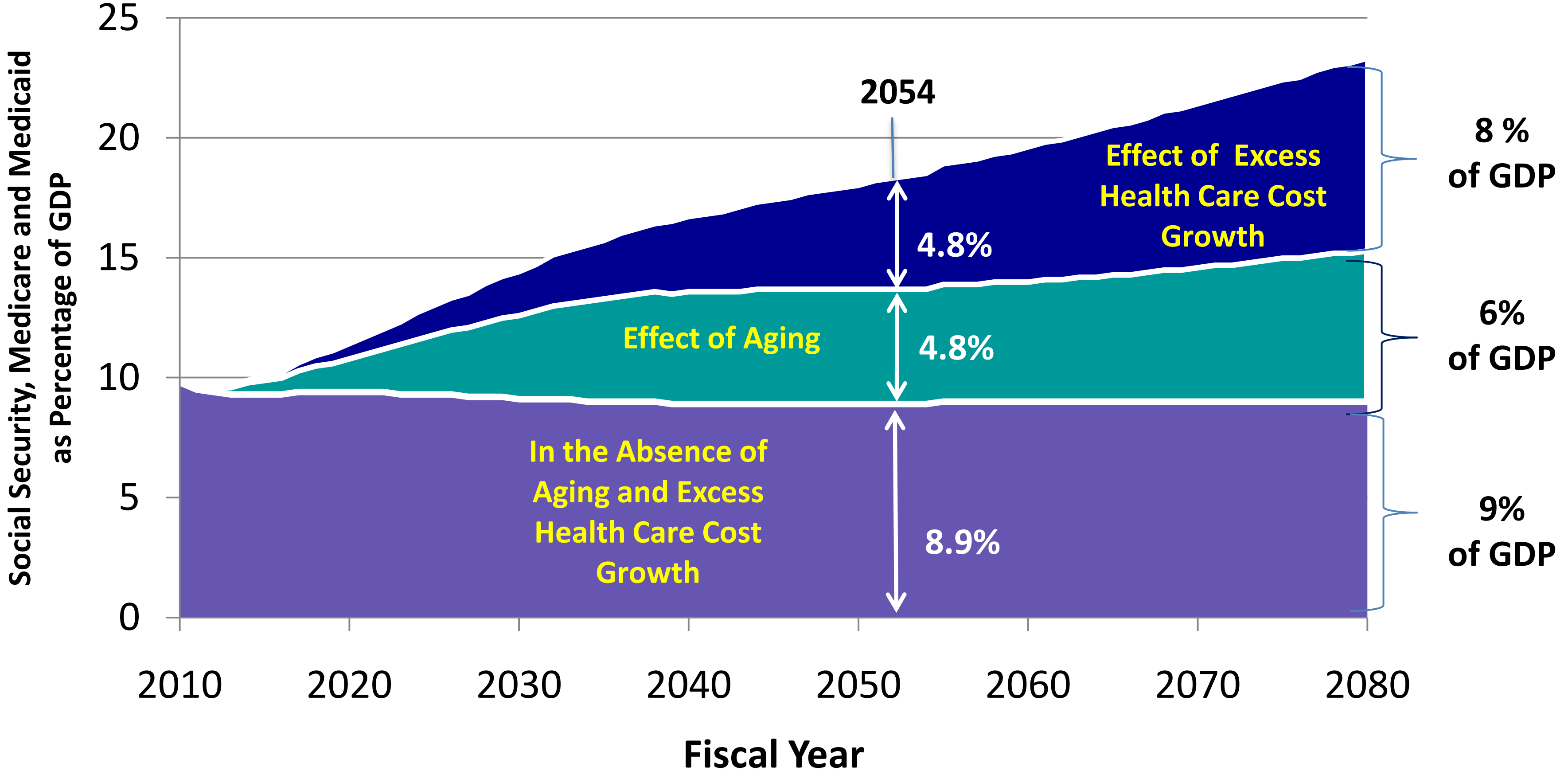
Aging drives most of the projected cost growth in Social Security, Medicare, and Medicaid until 2054. After that year, health care costs takes over as the leading driver of spending growth.



SOURCE: Data from the Congressional Budget Office, *The Long-Term Budget Outlook* (June 2009). Compiled by PGPF.
NOTE: "Excess health care cost growth" is the amount growth in age-adjusted health care costs per person exceeds the growth in per capita GDP.

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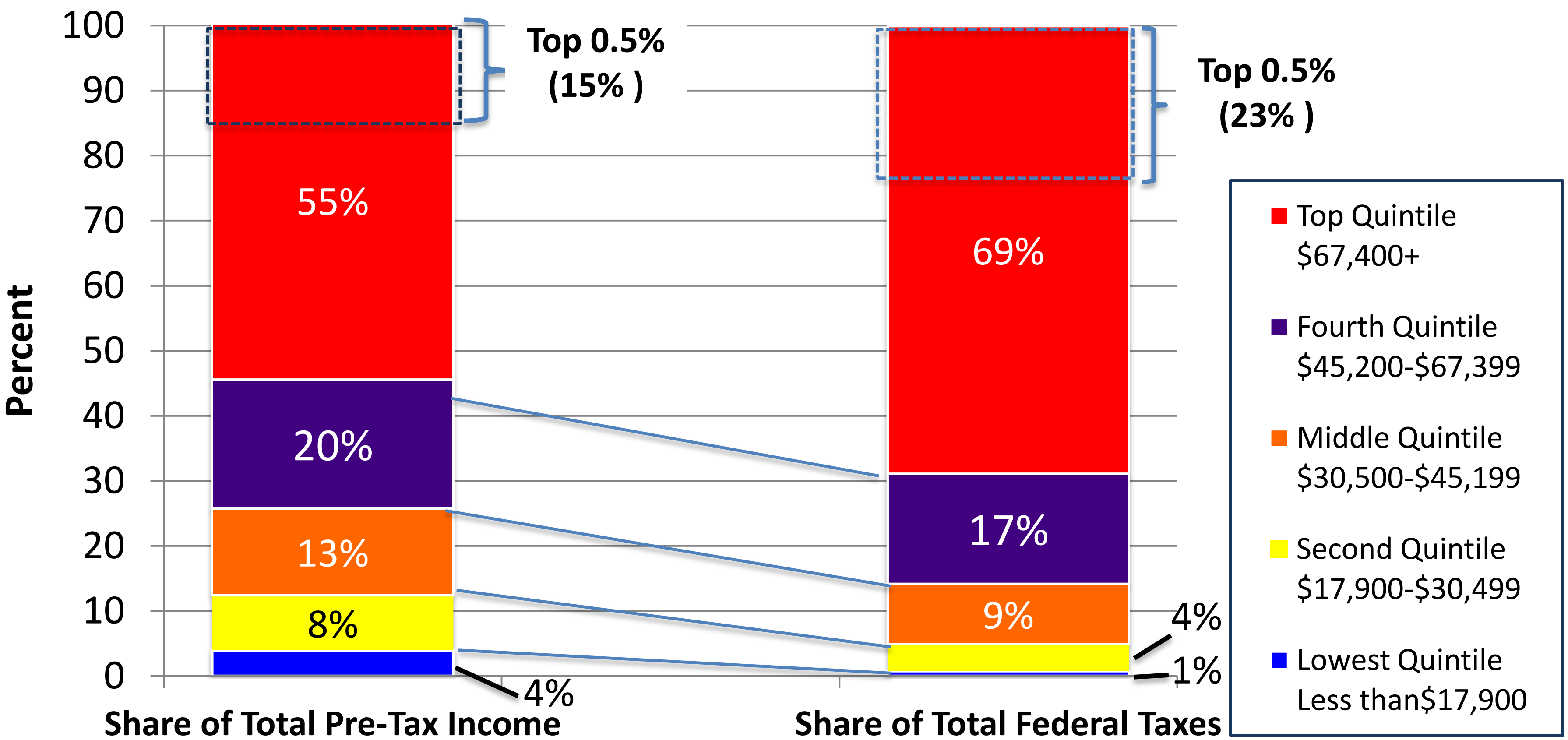
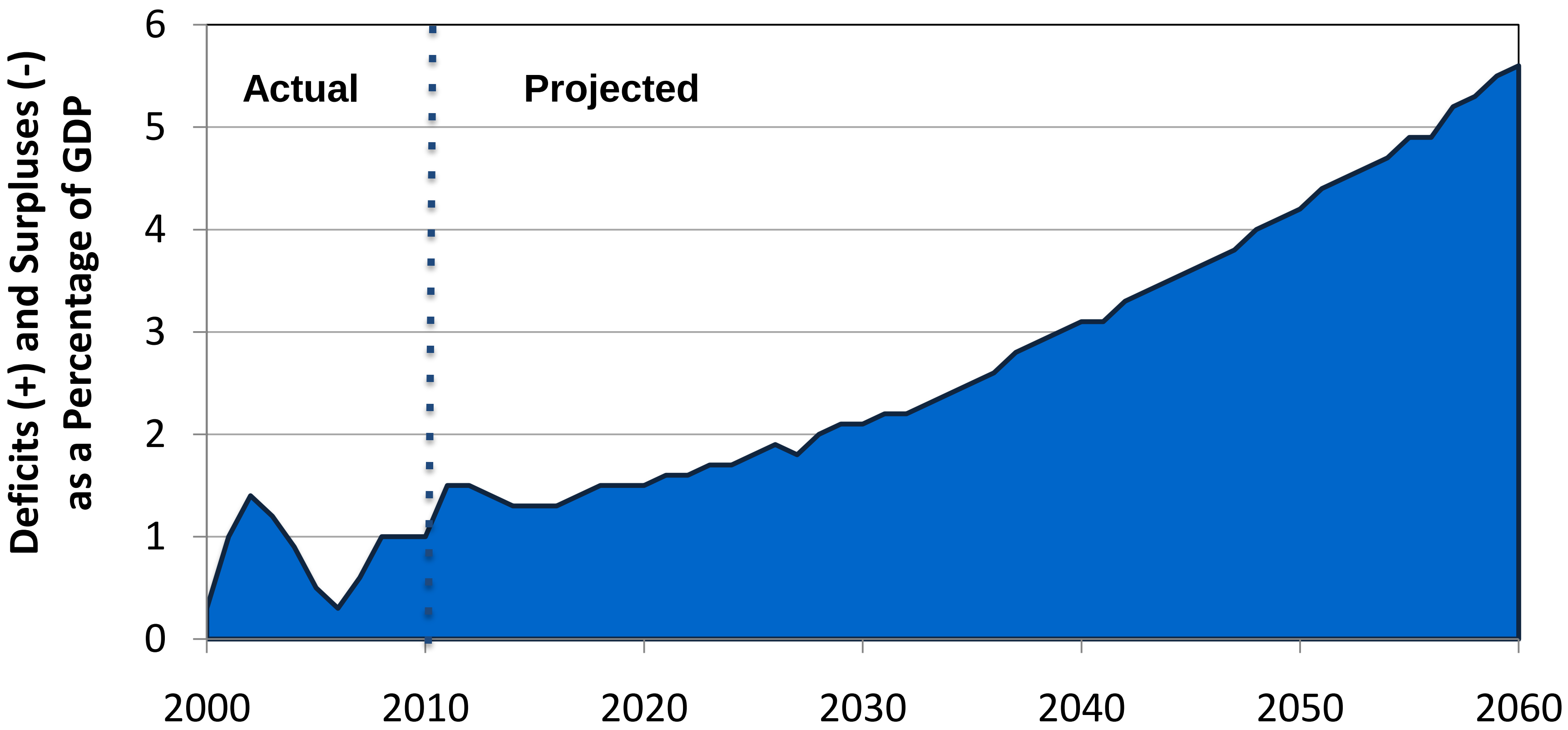
High-income households earn a disproportionate share of pre-tax income and pay a disproportionate share of total federal taxes



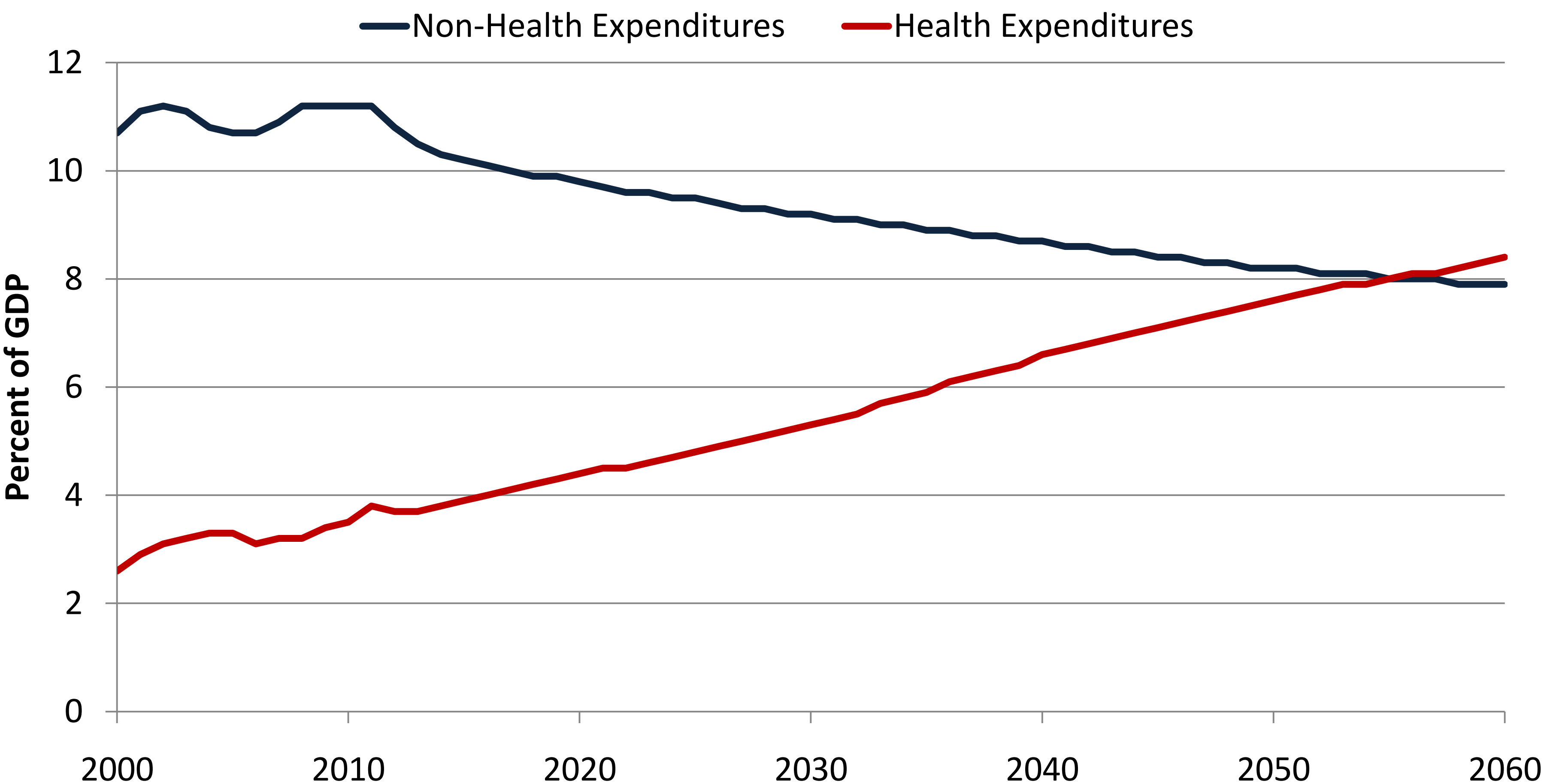
SOURCE: Congressional Budget Office, *Historical Effective Tax Rates: 1979- 2005: Additional Data on Sources of Income and High-Income Households* December 2008. Compiled by PGPF.
NOTE: Data for 2005 in 2005 dollars.

Under current policies, state and local deficits are projected to more than double as a percentage of GDP, even after the economy recovers



SOURCE: Data from the General Accountability Office *State and Local Government's Fiscal Outlook* March 2010 Update. Compiled by PGPF.

Future state & local expenditures on health care are the primary source of their poor fiscal outlook.



SOURCE: Data from the General Accountability Office *State and Local Government's Fiscal Outlook* March 2010 Update. Compiled by PGPF.
NOTE: State level health expenditures are primarily Medicaid and health insurance for government employees and retirees.

Unfunded Federal and State Employee Retirement Liabilities in Fiscal Year 2008

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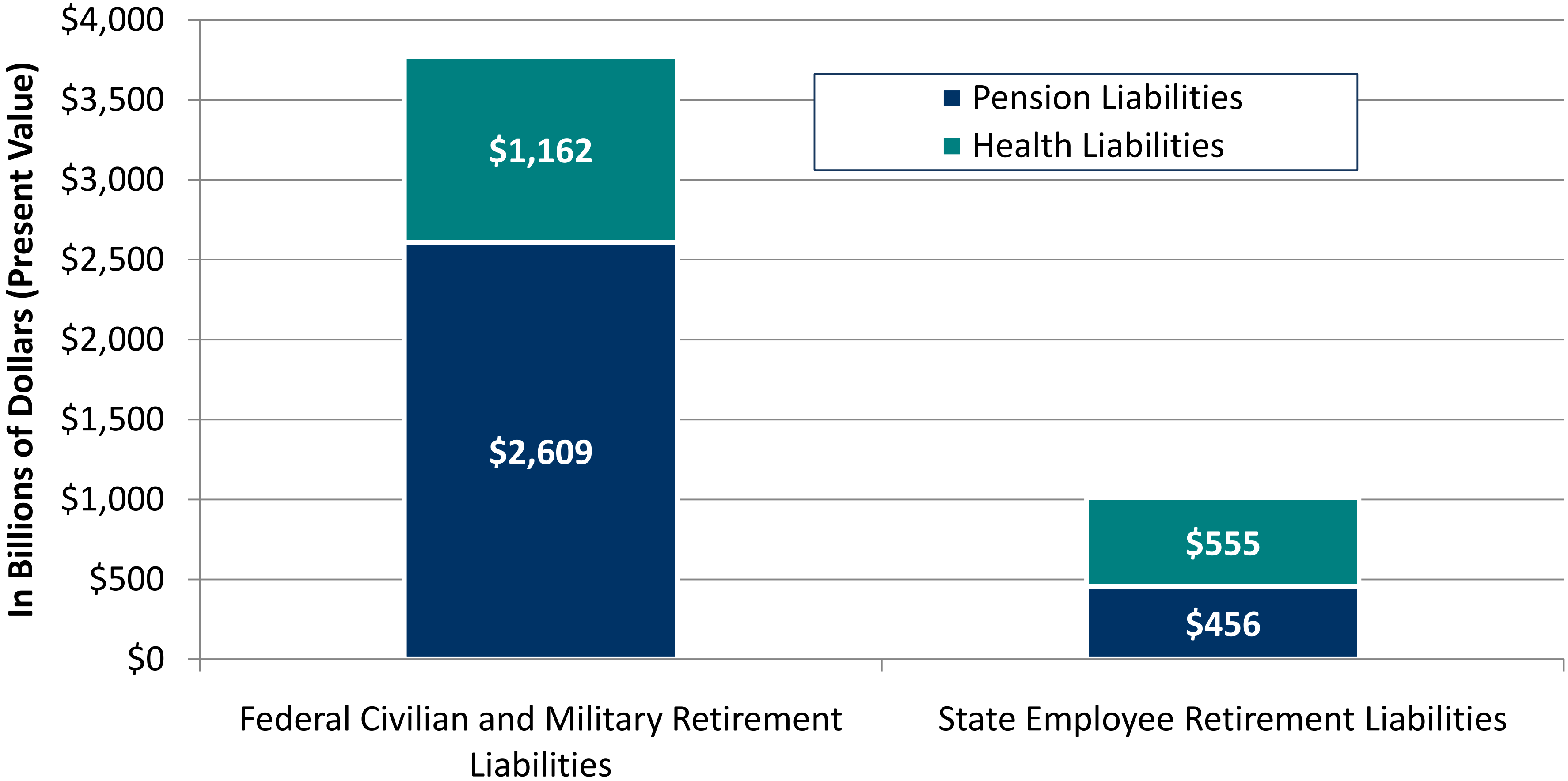

SOURCE: Pew Center on the States, *The Trillion Dollar Gap* February 2010; U.S. Treasury Department *Financial Report of the U.S. Government* 2008.
NOTE: Data is as of the end of fiscal year 2008. The unfunded liability is the difference between the present discounted value of future liabilities and current assets. For the purposes of converting future liabilities into present value, most states use a discount rate of approximately 8%, based on assumed returns on investing their pension funds.

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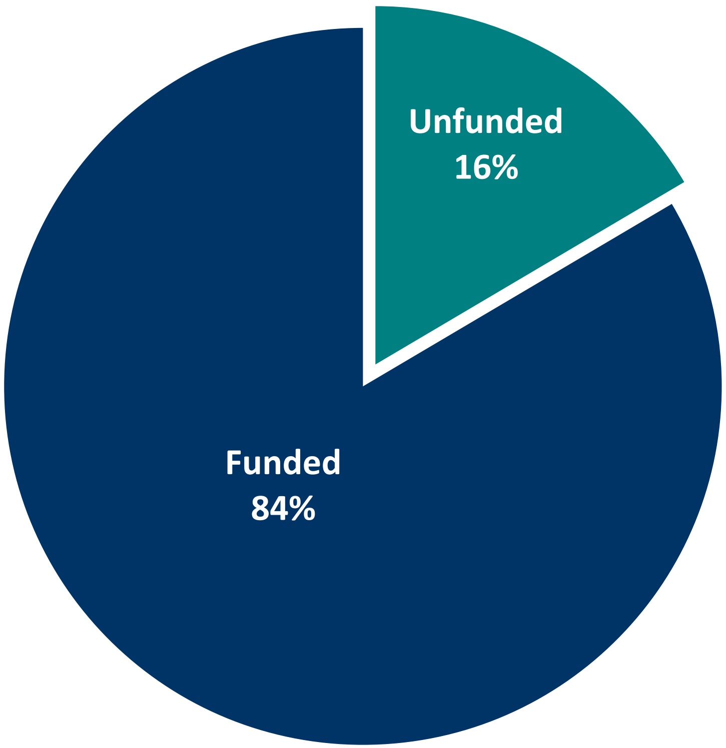
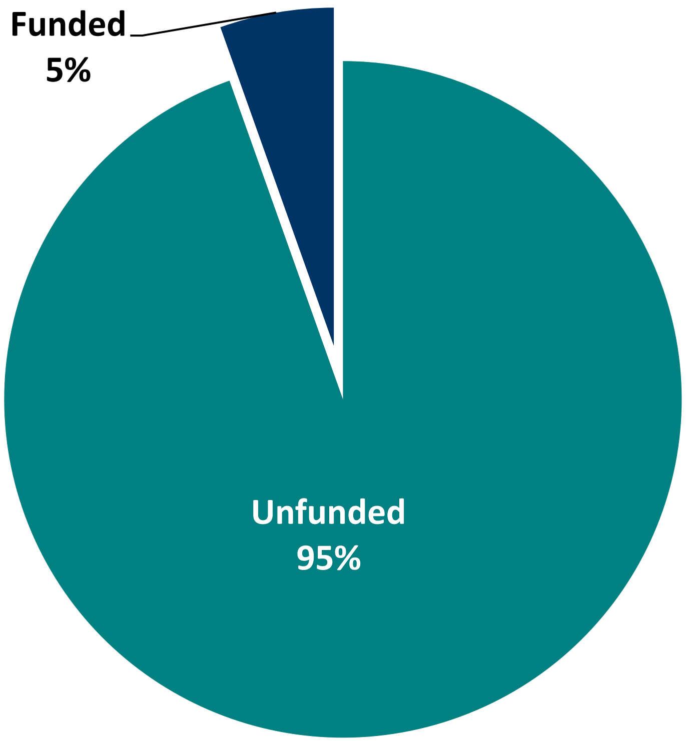
Federal and State Employee Retirement Liabilities in Fiscal Year 2008

State Pension Liabilities

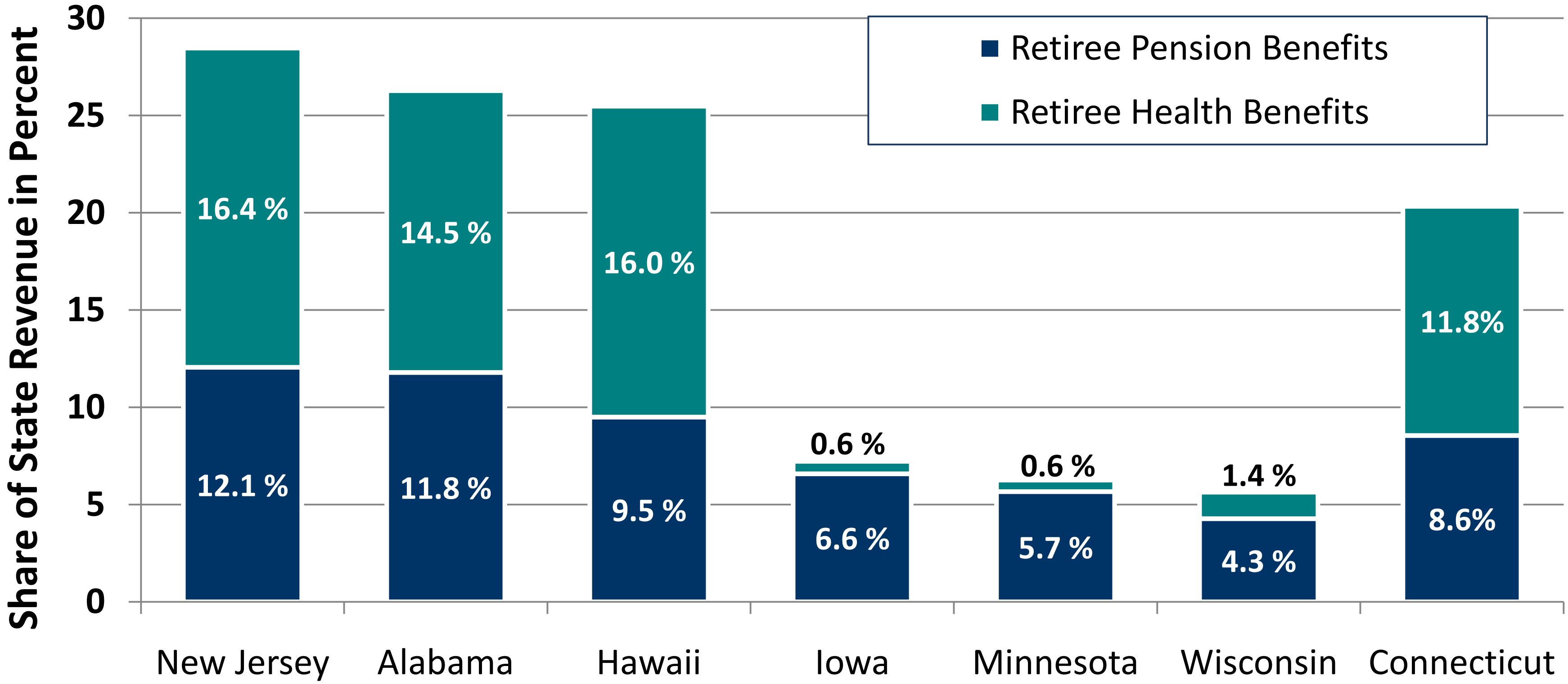


State Health Liabilities



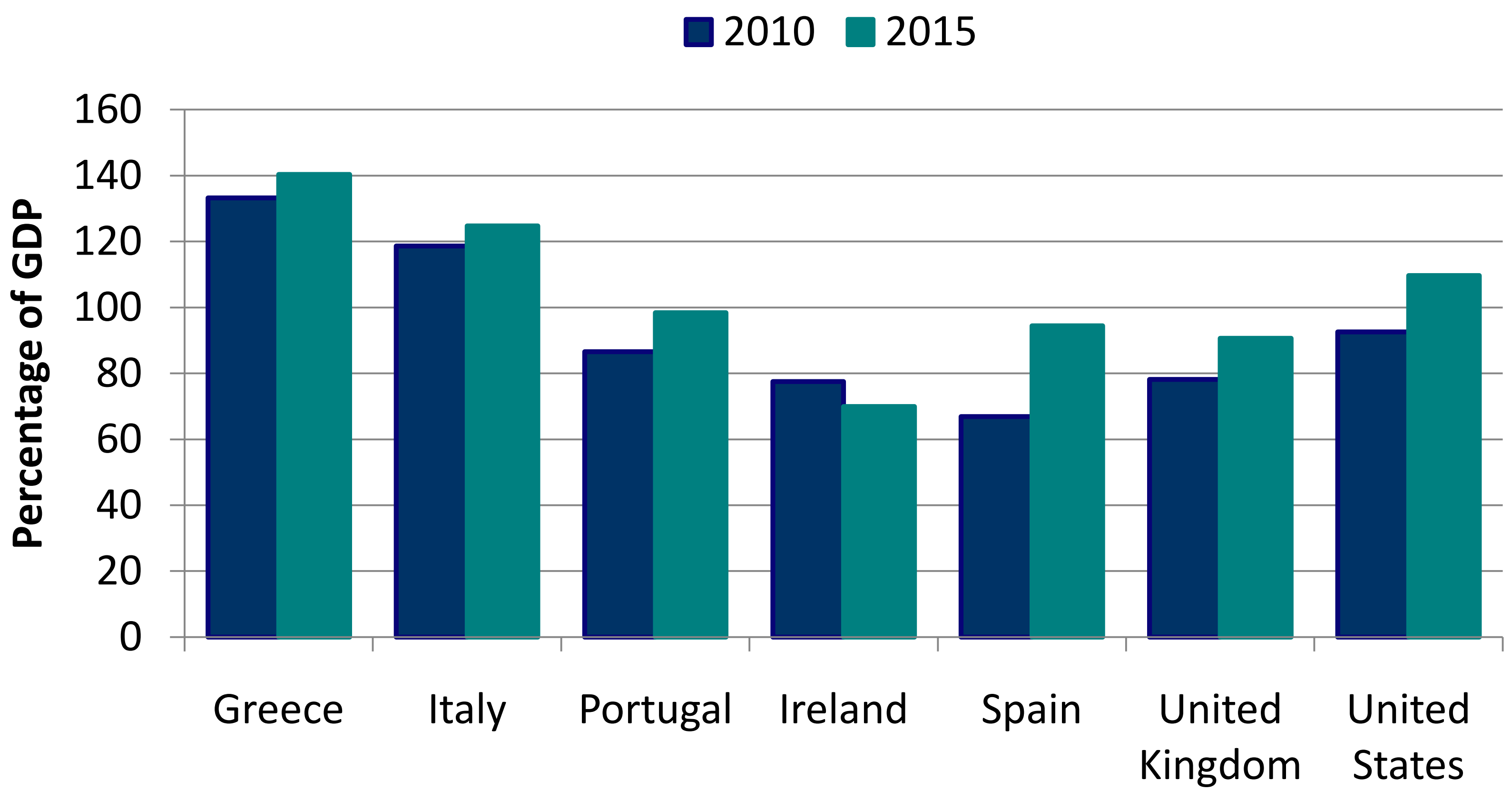
SOURCE: Pew Center on the States, *The Trillion Dollar Gap* February 2010; U.S. Treasury Department *Financial Report of the U.S. Government* 2008.
NOTE: Data is as of the end of fiscal year 2008. The unfunded liability is the difference between the present discounted value of future liabilities and current assets. For the purposes of converting future liabilities into present value, most states use a discount rate of approximately 8%, based on assumed returns on investing their pension funds.

Actuarially Required Contribution to Retiree Health and Pension Funds (as a Share of State Revenue) in Fiscal Year 2008



NOTE: The actuarially required contribution is the annual contribution to the retiree pension and health funds required for future assets to be in line with future liabilities within 30 years. It has two components: a normal contribution to keep up with new benefit obligations accrued, and a catch-up payment to make up for the current gap between pension assets and liabilities. The data for both revenues and unfunded obligations are for fiscal year 2008. Most states end their fiscal year in June of 2008, and therefore these numbers do not include losses in the stock market that led to losses in most pension funds.

Total government debt in the U.S is higher than some of the most financially troubled countries in Europe



SOURCE: Data from the International Monetary Fund, *IMF Fiscal Monitor Series: Navigating the Fiscal Challenges Ahead* (May 14, 2010). Compiled by PGPF.

NOTE: Both 2010 and 2015 figures are estimates. Total government debt (also referred to as general government gross debt) measures all liabilities that require payment or payments of interest and/or principal by the debtor to the creditor at a date in the future. This includes central, state, and local government debt.

Moody's Rating Structure

Obligation Rating		
	Aaa	
Aa1	Aa2	Aa3
A1	A2	A3
Baa1	Baa2	Baa3
Ba1	Ba3	Ba2
B1	B3	B2
Caa1	Caa2	Caa3
	CA	
	C	

Top Rating/
Minimal Risk

Bottom Rating/
Typically in Default

SOURCE: Data from Moody's Investors Service, Government-Related Issuers: Methodology Update, July 22, 2010. Compiled by PGPF.

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State and City Moody’s Ratings

State	City
Georgia –Aaa	Alexandria, VA - Aaa
Texas - Aaa	Jacksonville, FL – Aa1
Virginia -Aaa	San Francisco – Aa1
Alabama – Aa1	Atlanta – Aa2/A1
Florida –Aa1/Aa2	Washington – Aa2/Aa1
Connecticut - Aa2	Chicago – Aa2
New York – Aa2	Houston – Aa2
New Jersey –Aa2/Aa3	New York – Aa2
California – A1	Bridgeport, CT - A1
Illinois - A1	Miami - A1

SOURCE: Data from Moody’s website, Look-up a Ratings. Compiled by PGPF.

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Key Systematic Factors Driving Deficits and Debt at the Federal, State and Local Levels of Government

- Expansion of government at all levels
- Health Care Costs
- Retirement Income Costs
- Disability and Welfare Related Costs
- Critical Infrastructure Needs
- Education Costs
- Outdated and Inadequate Revenue Systems
- Myopia, tunnel vision, special interests and self-interest.

The Way Forward

Federal:

- Implement statutory budget controls that address discretionary and mandatory spending as well as tax preferences in order to stabilize our debt/ GDP at a reasonable level
- Achieve Social Security reform that makes the program solvent, sustainable, secure and more savings oriented
- Reduce the rate of increase in health care costs and more effectively target related taxpayer subsidies and tax preferences
- Ensure that all future health care reforms adequately consider coverage, cost quality and personal responsibility

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The Way Forward- Continued

- Pursue comprehensive tax reform that makes the system more streamlined, understandable, equitable and competitive while also generating adequate revenues

- Review, re-prioritize and re-engineer the base of the federal government to focus on the future and generate real results

- Ensure that we have process that will enable us to achieve the above objectives within a reasonable period of time

State and Local:

- Reform pension and health systems to make them reasonable, affordable and sustainable
- Review, re-prioritize and re-engineer the base of government.
- Pursue comprehensive tax reform in coordination with the federal government.
- Consider an exchange of primary roles, functions and revenue sources as part of a new federalism or devolution effort (e.g., health care, education, infrastructure)